



ECOSOC 2010

High-Level Policy Dialogue
with the international financial and trade
institutions on current developments in
the world economy

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Statement by

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Excellencies,
Distinguished delegates,
Ladies and gentlemen,

The past decade was an optimistic period for developing countries and for their development partners. Economic growth rates achieved record heights – exceeding 5% even in poverty-strapped sub-Saharan Africa – and after a decade of stagnation, aid flows began to rise. The MDG initiative to tackle poverty and related development challenges through a set of internationally agreed development targets certainly galvanized donor country support. Since the recent financial crisis, however, economic growth has shrunk. The impact has been severe, not just on poor developing countries in great need of aid, but also in donor countries that are coming under increasing fiscal pressure to cut their aid budgets. Prospects for achieving the MDGs by the 2015 target date look dimmer than ever.

We must remain focused on poverty and redress inequalities

Prospects are especially bleak for MDG 1, halving the number of people living in extreme poverty. Even before the crisis hit, the rapid economic growth of the past 10 years had failed to staunch rising inequality, which is frequently associated with poverty. In fact, the evidence indicates that economic growth may even worsen the situation of vulnerable people and communities where income distribution is unequal. The policy implication is clear: making economic growth more inclusive – clearly a prerequisite to achieving all the goals – requires placing public investment in productive sectors, employment and income distribution on an equal footing with price stability in the design of more inclusive development strategies. Indeed, there is increasing evidence that greater inclusion is also good for economic growth.

The past 10 years have seen a massive transfer of wealth, whether through taxation, the socialization of risk, low or stagnant wage growth among

sustained; it is, in the long run, crucial to attaining all the MDGs. Increasing the share of productivity gains that have accrued to workers will be one way to more fairly distribute the benefits of globalization and boost consumption through higher wages. But we also need to look at more radical measures for redressing the wealth transfer from vulnerable and low-paid workers in the real and informal economy to high-wage earners in the casino activities of the financial economy. Among other things, this may be achieved through debt rescheduling – a subject I will return to later.

Current trends in the global economy

With developing countries leading the recovery, the policy-sponsored upturn in developed countries remains fragile and uneven. In a repeat of global pre-crisis patterns, the United States has been experiencing a stronger recovery in domestic demand than the leading developed surplus countries. But in moving forward, the United States is likely to face strong headwinds as its fiscal stimulus peters out in the course of 2010, with fiscal austerity measures spreading at the state and local government levels as balanced-budget rules bite. Although originating in the United States, the global crisis has now become Europe-centred, and the continent is acting as a drag on the global recovery. With the prospect of a premature removal of stimulus in Europe, the risks of a European or even global double-dip recession are perceived as rising. The unfolding of events in the world's foremost trading region poses a formidable global threat. In the eagerness to embark on consolidation, people forget that a double-dip recession resulting from the retreat from expansionary policies would pose the greatest threat by far to public finances.

At the peak of the global crisis, G20 members managed to see eye-to-eye on the need for coordinated measures as the sheer severity of events necessitated only the most extraordinary coordinated action on stimulus measures from these countries. Apparently that moment has passed. Shared views and diagnoses of challenges seem harder to reach as important conflicts in policy visions have re-emerged. The Euro area believes that rather than harming growth, fiscal austerity would support it, by boosting confidence. In the United States, by contrast, the prevailing fear is that continued domestic demand stagnation in Europe may threaten the recovery.

The European view rests on an extreme set of assumptions. The supporting evidence for their position consists of small-country experiences featuring currency depreciation and sharply falling interest rates. A fallacy of composition is involved in applying the experiences of individual small

countries to the case of continent-wide austerity. In the current situation, the "short-run" effects of fiscal austerity, including job losses, are unlikely to be offset by sharply falling interest rates and improved confidence about long-run prospects. And Euro depreciation essentially means exporting deflation from an economy nearly as large as the US to the rest of the world. Instead, failure to coordinate policies effectively at the global level raises the prospect of re-emerging global imbalances, especially among developed countries.

for their products, and to protect
external shocks, but to allow

At the national level, to allow wage
encourage consumption, help demand and employment, the
key factor for the sustainable poverty reduction envisaged by

and here I am referring specifically to China and other Asian nations
can also help rebalance the huge asymmetries in foreign reserves. The
current withdrawal of around US\$7 trillion from the world economy, which
is being held as a form of self-insurance in foreign exchange reserves,
represents a giant loss of demand for the world economy, and developing
countries in particular, at a time when it is most needed. Rebalancing
reserve holdings, along with wage growth, are two areas that could have an
immediate but sustainable impact on demand and ultimately on poverty
reduction.

The correct response to current global economic conditions, therefore, is
not to freeze or reduce wages, or to increase taxation, which would punish
the most vulnerable, but to invest in growth, most probably through deficit
spending and investment in productive capacities. This is the most efficient
way to tackle poverty and to reverse the impact of the crisis on the poorest,
which has severely affected the trajectory of efforts to meet the MDGs.

Not the right time for fiscal austerity

The bond markets have indeed got governments scared, but large deficits
during a contractionary or sluggish growth phase are the sign of attempts
to resuscitate demand. Conventional wisdom suggests we should be wary
of large deficits. But we are living in unconventional times, and our
priorities are to protect the most vulnerable, and not just the profit
margins of wealthy corporations. Deficits only become truly dangerous
when there is a double-dip recession as a result of fiscal rectitude. This is
exactly what happened to the United States in 1937, when Treasury
Secretary Henry Morgenthau thought it timely to reduce government
spending. The result was a calamitous descent back into recession – a
descent arrested only by the outbreak of the Second World War.

Clearly, then, this is not the time to be cutting deficits. In the current
situation, any withdrawal of policy stimulus remains a highly delicate
matter: In many countries, private demand has so far only partially
recovered from its trough and, remaining fragile, is nowhere near its pre-
crisis levels. This is especially true for Europe, the world's foremost

trading region. Premature national or regional exits from domestic demand-supporting measures could render countries or regions over-reliant on exports for their growth. The stimulus burden to be carried by the remaining countries at the regional or global level would then rise accordingly. Re-emerging global imbalances and protectionism could be the consequence.

The global economic crisis and immediate policy responses saw a shrinking of imbalances. But if the global economic forces that gave rise to imbalances prior to the crisis reassert themselves, rising imbalances will also re-emerge in due course. Strong domestic demand growth in developing countries, led by China, together with strengthening currencies, contributes to global rebalancing. But forces working toward global imbalances emanating from developing countries may see some revival owing to developing countries' need to self-insure. Imbalances among advanced economies risk becoming even greater, due to relative domestic demand growth developments that are amplified rather than offset by the weakness of the Euro.

Developing countries need help with their debt positions

For developing countries, sovereign debt can become an unsustainable burden. In some countries, debt servicing alone absorbs 40% of their aid receipts – money that would be far more wisely spent on investment in productive capacity and job creation. UNCTAD has been calling for the creation of a multilateral debt work-out mechanism to ease the burden on poor countries and to bring some coherence to development assistance in general. Debt rescheduling and the better management of debt, including postponing debt repayments and declaring moratoriums on debt, could help countries support their economic growth and increase government support their economic growth.

As I said at the time, the economic crisis has meant that we are not achieving the Millennium Development Goals. The goal of halving poverty by the end in 2015. Yet, it might even be possible to achieve this goal if we had a faster and more effective response. At UNCTAD, we believe that the Millennium Development Goals should be better aligned with development strategies. In the first place, this means making countries masters of their own destinies. They need to increase their

make growth more inclusive. In the second place, this calls for strong States with a developmental vision. This is not to imply that there is no role for the market, nor that State control solves all problems. But experience has shown that the most successful policies are those that strike the right

and pragmatic balance between the State and the market. Such policies are aimed at economic diversification, infrastructure development, skill formation, social safety nets and private-sector development.

Thank you.

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